

Encouragement of raw materials processing

- 6.1 Australia has a number of underlying advantages that should assist it to draw on its strong raw materials base to enhance its productive capacity. It is unlikely this potential will be fully realised, however, unless there are policies in place which foster value-adding activity.
- 6.2 As indicated by ABARE:
- The location of mining and mineral processing activities is influenced by decision making in both the private and public sectors. Mining and mineral processing companies locate activities to maximise profit over time, taking into account the various costs and risks associated with different sites. Government policies may influence location decisions by altering the industry assessments of the economic viability of particular projects.¹
- 6.3 A number of witnesses identified a range of possible actions that could be adopted by both government and industry to foster this activity. These actions are discussed in this chapter and range from providing a conducive economic environment and enhanced labour skills through to the removal of a series of impediments.
- 6.4 In the next stage of the inquiry, the Committee will undertake industry case studies to solicit further evidence on these and other actions to encourage value-adding.

¹ ABARE, submission no. 42, p. 5.

Conducive economic environment

6.5 A number of witnesses suggested that the realisation of Australia's full raw materials processing potential requires a sound macroeconomic environment that is conducive to business and facilitates change. The Department of Industry, Science and Resources, for example, suggested:

Raw materials processing tends to involve large scale, capital intensive investments which have long effective lives and relatively long gestation periods. It is therefore essential to have an efficient, vibrant, competitive, predictable and stable economy if Australia is to attract such investment and to ensure that its existing industry remains viable.

While many raw materials processing projects will benefit from being located close to the source of supply of raw materials, many are less dependent on this factor and indeed have a wide range of choice as to where they locate. To attract these plants (and indeed to assist the viability of those that benefit from location close to the source of supply), Australia needs to ensure that it maintains sound monetary and fiscal policies so that its economic environment is conducive to these businesses.²

6.6 The Committee agrees with this assessment. Sound monetary and fiscal policies are necessary prerequisites to encourage investment in any industry in Australia.

6.7 As discussed in Chapter 5, a stable and efficient economic environment is an important attribute in making Australia an attractive place to invest. It can play a very important part in enhancing the viability of local industry and in contributing to a competitive advantage for Australian industry in world markets.

6.8 It is therefore important for Australia to have a favourable environment which offers factors such as competitive interest rates, a stable exchange rate, low inflation, a healthy capital market with ready access to foreign capital and a well-developed competition policy.

Microeconomic reform

6.9 Many witnesses advocated on-going microeconomic reform, suggesting that any underlying comparative advantage in raw materials processing will only be fully realised if industries have access to inputs at world competitive prices. The Minerals Council, for example, claimed:

Sound macroeconomic management and a vigorous and continuous program of microeconomic reform is the key to encouraging further processing of minerals in Australia. For example, tariff reforms, both at home and abroad, and transport, energy and industrial relations reforms, increase opportunities for further processing in Australia by improving the economic viability of such activity which is inherently risky given the high volatility of prices of refined metals.³

6.10 In supporting this thesis, others such as the Western Australian Government and DFAT noted the positive impact that such reform was already having on raw materials processing activity. The Western Australian Department of Resources Development suggested:

The Western Australian Government's commitment to microeconomic reform in the energy, labour and transport sectors, coupled with rapid advancements in technology, provide increasing potential for more processing industries in Western Australia. Recently completed and planned value-adding projects will greatly increase the level of downstream processing of the State's rich supply of raw materials over the next decade.⁴

6.11 DFAT claimed:

Wide-ranging microeconomic reforms have also fundamentally changed the structure of the Australian economy and made many sectors more efficient, flexible and productive. Obvious areas of improvement include the labour market, banking, finance, transport, public utilities, provision of many government services and the waterfront. These reforms have reduced the costs and increased the productivity of our manufacturers and enabled many of them to compete more effectively in export markets. The result has been a strong increase in manufacturing exports.⁵

3 Minerals Council, submission no. 13, p. 2.

4 Western Australian Department of Resources Development, submission no. 37, p. 1.

5 DFAT, submission no. 32, p. 12.

- 6.12 The Committee acknowledges the important part that microeconomic reform has played in enhancing the efficiency of Australian industry, and agrees that the prospects of Australia's raw material processing industries will be improved through well-focussed continuing reform.
- 6.13 The future of these industries in Australia will be highly dependent on access to competitively priced inputs, such as electricity, gas, rail and sea transport. Microeconomic reform helps to achieve this by lowering input costs, increasing productivity and increasing competition in supplier industries.
- 6.14 The vital importance of this reform is well demonstrated in a number of reports. For example, the Industry Commission has noted that minerals processing is usually energy intensive, with energy costs of some processors constituting up to 40 per cent of variable operating costs.⁶
- 6.15 The Centre for International Economics has developed this theme further, suggesting:

The importance of microeconomic reform in enhancing prospects for further processing is illustrated by the dramatic falls in energy costs ...the deregulation of the gas market in the Western Australian Pilbara region is providing a strong stimulus to further processing of minerals.⁷

Sovereign risk

- 6.16 Another issue that has an important bearing on the attractiveness of Australia as an investment location, particularly for investment in mineral-related activities, is the question of sovereign risk. The submission from the Association of Mining and Exploration Companies outlines this concern:

The term 'sovereign risk' refers to the likelihood that the Government (State and/or Federal) with jurisdiction over the project will change the operating environment or 'rules', midway through the project development process.

It is not difficult to understand why sovereign risk represents such a significant factor in company decisions to invest large capital sums. To invest what are often enormous sums of money in resources projects, company directors with responsibility for

6 Industry Commission, *Mining and Minerals Processing in Australia*, February 1991, Volume 1, p. 141.

7 Centre for International Economics, exhibit no. 7, p. 7.

shareholders funds must be confident that the legislative and regulatory environment, as administered by the relevant government(s), will not undergo dramatic change resulting in unexpected time delays, increased company compliance costs and possible permit withdrawals.⁸

6.17 ISR added:

Industry argues that it needs to be confident in government policy and decision making processes if it is to risk its capital on long term investments in Australia. Among the issues affecting investment decisions in these areas are resource access and environmental constraints, including greenhouse gas emissions policy.

Industry is looking for a consistent, long term policy approach to its activities, under which investment can be made in a timely manner and with a minimum of administrative process. It believes, in particular, that the minimisation of the delays associated with granting access and gaining approvals will greatly assist investment activity in this area.⁹

6.18 While the Committee agrees that an open and efficient regulatory framework will help promote investment in Australia, it also recognises the need for a balanced approach in this area. There are often good reasons for planning, access and environmental controls and it is therefore necessary to strike an appropriate balance between these issues and the broader goal of encouraging raw materials processing.

6.19 The application of these policies, however, should be undertaken in a consistent manner so that industry is well aware of the ground rules. Industry will only be willing to risk the often substantial sums involved in raw materials processing projects if the rules and regulations are clear and if it has confidence that they will not be significantly changed during the life of a project.

Trade issues

6.20 Trade barriers can also play a major part in influencing industry viability. The potential impact of tariffs on minerals processing in Australia was raised, among others, by the Centre for International Economics:

8 AMEC, submission no. 25, p.24.

9 ISR, submission no. 28, p. 16.

Tariff policies in Australia and other countries can considerably influence further processing. In Australia, tariffs against manufactured imports restrict competition, increase inefficiencies, add to the economy's costs and reduce the international competitiveness of mining and minerals processing. Trade barriers overseas also influence prospects for further processing of minerals in Australia.¹⁰

- 6.21 The Department of Industry, Science and Resources discussed the potential impact of a wider range of trade barriers in its submission to the Committee:

Trade barriers of different types can also work to harm the competitiveness of existing and potential raw materials processing industries. While the tariffs on early stage processed products are generally relatively low, as noted by EPAC,¹¹ this can still confer a significant level of effective protection when the level of value adding is only modest, as indeed can non-tariff barriers. Furthermore developing and newly-industrialising nations often assist the development of their export processing industries in a variety of other ways, including the underpricing of energy and various substantial tax advantages and incentives. Trade in processed food is also still constrained by the agricultural policies of the industrialised countries.

Given that all these measures can significantly reduce the opportunities to further export value added product, countries such as Australia, that appear to have significant advantages in raw material processing, need to take continuing and meaningful action against these measures.¹²

- 6.22 The need to take action in these areas was also reinforced by the evidence the Committee received on the level of 'tariff escalation' in some of Australia's trading partners.¹³ It appears many countries apply higher tariffs to processed goods than raw products and this works to further discourage trade in value-added products.
- 6.23 In view of the impact that these measures are having on Australia's value-adding potential, the Committee strongly supports the suggestion that Australia needs to take robust action against them. If raw materials processing is to be progressed, Australia needs to continue to work for the reduction of all the barriers to free and open trade.
-

10 CIE, exhibit no. 7, p.7.

11 EPAC, *Raw Materials Processing: Its Contribution to Structural Adjustment*, April 1988, p. 27.

12 ISR, submission no. 28, p. 18.

13 See, for example, DFAT, submission no. 32, pp. 13-14.

- 6.24 The Department of Foreign Affairs and Trade outlined the range of approaches being used by the Government to realise this objective.¹⁴ These include multilateral negotiations through the World Trade Organisation, regional approaches through forums such as Asia Pacific Economic Cooperation (APEC) and bilateral negotiations with individual countries.
- 6.25 Significant gains in access has been achieved, for example, through the Uruguay Round of multilateral trade negotiations (including reduced tariffs on industrial products) and from the commitment by APEC nations to free and open trade and investment in the Asia-Pacific by 2010 (2020 for developing countries).
- 6.26 Australia's efforts in all these areas should continue unabated, with the broad aim of quickly reducing all tariff and non-tariff barriers to Australia's exports of processed raw materials.
- 6.27 At the same time, Australia will need to continue to assist its companies to enter new markets and to expand their presence in existing markets. This assistance, which is usually provided through the Austrade worldwide network, can involve both helping local companies to identify export opportunities in overseas markets and in realising these opportunities. This can include helping with the establishment of appropriate contacts and distribution networks and with the marketing of goods and services.
- 6.28 The Committee invites comment on the effectiveness of the assistance that has been provided in developing new markets and on alternative methods of assistance.

Research and development

- 6.29 Another issue that can have a significant impact on competitiveness at the industry level is research and development. As suggested by the Process Engineers and Constructors Association:

In the mining sector, the need for innovation to maintain a competitive industry is critical. R&D is ensuring that new deposits are discovered and new technologies are making the development of more projects economic to undertake. New and innovative approaches to mining have made many mineral deposits economically viable.¹⁵

14 DFAT, submission no. 32, pp. 16-19.

15 PECA, submission no. 16, p. 4.

6.30 Goodman Fielder noted the importance of research and development for the success of the food processing industry:

Product innovation in mature industries such as food processing is as important as innovation in high technology or telecommunications industries. Indeed it can create sustainable competitive advantages and new industries.

Successful product innovation however requires a strong commitment to long term research and development.¹⁶

6.31 The Queensland Government suggested that countries with a positive balance of trade in high growth industries are those which make substantial investment in research and development.¹⁷

6.32 The Committee agrees that research and development can play an important part in the development of raw materials processing. Indeed research and development is often the very key to investment in these industries.

6.33 By its nature, raw materials processing is usually a technology-based business. Product and process innovation can be critical to the development of these industries in Australia and can be the very issue that brings them to fruition and makes them competitive on the world scene.

6.34 In addition, process innovation in itself can provide a strong basis for Australian exports and additional income for Australian companies. The intellectual 'know how' associated with research and development is becoming an increasingly important source of industry income, as was noted by the Association of Mining and Exploration Companies:

By 2005, it is estimated that Australian mining intellectual property or 'know how' will be Australia's fifth largest mineral export behind coal, gold, aluminium and iron ore, and it will be level-pegging with the wool, wheat and beef industries.

Furthermore, according to one forecast cited by Mr Cribb,¹⁸ Australia will be world dominant in this field by 2020.¹⁹

16 Goodman Fielder, submission no. 3, p. 6.

17 Queensland Government, submission no 43, p. 12.

18 Julian Cribb, Director of the CSIRO's National Awareness Program, in an address to the first Australian Minerals and Energy Environment Foundation Innovation Conference, March 1999.

19 AMEC, submission no. 25, p. 20.

Labour and skill issues

6.35 The Committee also received significant evidence on the importance of labour and labour-related issues for the future of raw materials processing in Australia. This evidence broadly covered two general themes: the need for effective and productive employee relations; and the need to have ready access to a highly skilled workforce.

6.36 The Australian Academy of Technological Sciences and Engineering provided a report to the Committee that included some comments on the first of these issues.²⁰ Noting that Australia's future competitors in the minerals industry are likely to have labour costs below Australia's, and that there is nothing it can or would want to do to alter this position, the Academy drew attention to the following comments from the Industry Commission:

Mining and minerals processing are generally capital intensive, employing labour that is relatively highly skilled and remunerated. In such cases, it is work practices, rather than labour cost levels which are important for unit labour costs. For example, it is typically important to have flexible working arrangements that allow equipment to be used more intensively and permit productivity based pay.²¹

6.37 The Department of Industry, Science and Resources added:

The labour issues of significance include such matters as downsizing (including the retrenchment process and redundancy payments), shift roster issues, annual leave provisions for continuous shift employees, performance management, workers' compensation issues, immigration provisions and issues relating to wages and conditions (particularly for new operations). The creation of flexibility within the industrial relations system is seen as the key to settling such issues with minimal industrial disputation.²²

6.38 On the need to have ready access to a highly skilled workforce, ACTED suggested:

The high profile and respected US based Michael Porter undertook a major survey of world industries and identified role models for government in Australia.²³ While disparaging of attempts by

20 AATSE, exhibit no. 5, p. 34.

21 Industry Commission, *Australian Direct Investment Abroad*, draft report, May 1996, p. 141.

22 ISR, submission no. 28, p. 18.

23 Porter, M.E. *The Competitive Advantage of Countries*, Macmillan Press Limited 1998

Government to directly promote industry, important roles were nevertheless identified. A key role was to promote the *quality* of education and training that Porter showed to underpin successful industries overseas some of whom lacked our natural resources. In countries such as Switzerland, Germany, Taiwan, the USA, education centres closely cooperate with industry to develop a robust industry that is less sensitive to exchange rates and economic cycles. A key role for Government should therefore be to help shape a skill base to promote excellence in chemical technologies with some remarkable precedents for success.²⁴

- 6.39 While acknowledging that there is likely to be on-going debate about the appropriate government response to these issues, the Committee agrees that productive labour relations and a skilled workforce can make an important contribution to attracting investment to Australia. Both issues can significantly contribute to an industry's competitiveness and can help it to fully realise its underlying comparative advantages.

Impediments to investment in raw materials processing

- 6.40 The option for encouraging competitive raw materials processing industries that received most attention in the evidence was the removal of impediments to investment.
- 6.41 Although many of these impediments relate to the broad policy issues discussed earlier in this chapter, they are both wide-ranging and diverse, and in some cases put another perspective on these issues.
- 6.42 The main impediments identified are therefore outlined below. It should be noted, however, that the Committee did not necessarily agree with all the actions proposed by witnesses. The Committee will further develop its views on some of these questions during the next stage of its inquiry.

Environmental issues

- 6.43 Perhaps the most common theme in the evidence related to government environmental controls. While some of this concern was directed at the interface between Commonwealth and State and Territory regulations, and in particular an alleged duplication of the environmental impact assessment processes,²⁵ most of the comments were directed at the greenhouse issue.

24 A.C.T.E.D. Consultants, submission no 29, p.5.

25 See, for example, AMEC, submission no. 25, p. 18.

6.44 In particular, a number of witnesses expressed considerable disquiet about the impact on business of the Kyoto Protocol to the UN Framework Convention on Climate Change. While generally acknowledging the greenhouse issue warrants a serious commitment by Australia, it was suggested the implementation of greenhouse controls has a very real potential to stifle value-adding to Australian raw materials.

6.45 The Australian Academy of Technological Sciences and Engineering, for example, claimed:

Assuming that full ratification of the Kyoto protocol proceeds, if Australia is to continue to increase its minerals processing capacity for products ultimately used by other nations, some way of offsetting the associated increase in emissions will have to be found... The matter is particularly vital for Australia, as if the matter is not resolved satisfactorily, value-adding opportunities could be lost by Australia, to nations not signatories to the protocol. Because the developing countries might well use less-efficient processes and fuels not as efficient or greenhouse-friendly as Australia's, the net global greenhouse effect could well increase.²⁶

6.46 A range of other witnesses endorsed this view including the Australian Aluminium Council, which indicated:

Of these challenges it is greenhouse that poses the greatest threat to future investment and the maintenance of prosperity of this industry in Australia. If the response to the greenhouse targets agreed at Kyoto is to substantially increase energy prices to the Australian aluminium industry then the value added sectors will become uncompetitive and the industry will be forced back to exporting basically the raw material. This is unlikely to have any global greenhouse benefit as the investment in the aluminium industry will go mainly to countries not covered by the Kyoto targets. In many cases these countries will use coal to generate their energy needs for such industries and in some cases may even base this on imports of Australian coal.²⁷

6.47 Although the Committee recognises that it is prudent for governments to introduce measures aimed at encouraging energy efficiency and minimising industry's environmental impact, it agrees that care needs to be taken in implementing such controls. Measures of this nature need to be implemented in a way that takes appropriate account of the broad range of government responsibilities, including the need to encourage

26 AATSE, submission no. 4.

27 Australian Aluminium Council, submission no. 31.

industrial development as well as the need to protect the environment for future generations.

- 6.48 The Committee is pleased to note that it received evidence on a future option that may contribute to this endeavour. The Fuel Ethanol Association of Australia provided a submission²⁸ outlining the prospects for a biofuels industry in Australia which could potentially provide substantial environmental, employment and wider social benefits.
- 6.49 Governments at all levels should be encouraging the development of environmentally sensitive options which can potentially contribute to the achievement of Australia's long term environmental objectives while also helping the development of regional areas.

Access to resources

- 6.50 Another common theme running through much of the evidence was that uncertainty about resource access has been creating impediments to the development of significant raw materials processing projects.
- 6.51 Most of this evidence was confined to two specific questions; the issue of resource security for the timber industry and the land access concerns flowing from the native title question.
- 6.52 The timber industry's concerns relate to its need to have adequate access and control over the supply, quantity and quality of raw timber. While the Regional Forest Agreement (RFA) processes were designed to address this issue, the industry believes progress has been too slow.
- 6.53 The National Association of Forest Industries, for example, suggested:
- ...at this time only four RFAs have been completed and there are a further eight outstanding. The timetable for completion of the RFAs has been revised many times with continual slippage in deadlines as a result of delays in completing technical work, additional requirements for stakeholder consultation and political expediency particularly the accommodation of election timetables....
- To date neither the Commonwealth or the states (except Tasmania) have provided legislative support to the RFAs and made commitments in relation to compensation which provide industry with a level of confidence required to encourage investment in further processing.²⁹

28 Fuel Ethanol Association of Australia, submission no. 35.

29 National Association of Forest Industries Ltd, submission no. 10, pp. 2-3.

- 6.54 Comments made to the Committee on the native title question related to the uncertainty the mining sector believes it faces in getting access to resources. For instance, the Western Australian Department of Resources Development suggested:

There remains considerable uncertainty at both the State and national levels over the passage and implementation of native title legislation. Until such time as these issues are resolved, doubts over security in relation to land access will act as a disincentive to potential investors in resource processing and other industries.³⁰

- 6.55 The Association of Mining and Exploration Companies added:

The realisation of state native title regimes has in practice however, proved fraught with difficulty due to the Federal Minister's approval of state regimes being subject to Federal Parliamentary disallowance....

Currently, over 12,000 Western Australian prospecting, exploration, mining and mining infrastructure tenement applications are stalled in the State's Department of Minerals and Energy system awaiting grant due to difficulties associated with native title. Furthermore, a considerable proportion of the 12,000 tenement applications referred to were lodged up to 4 years ago.³¹

Taxation

- 6.56 The issue of taxation also attracted considerable attention in the evidence received. These comments were generally centred on the claim that competitive fiscal regimes are required to compete internationally and to attract investment to Australia.
- 6.57 The Process Engineers and Constructors Association (PECA), for example, suggested:

The Government also has a role to play in providing a competitive tax system. The Australian tax system, currently the focus of debate, is not competitive and hinders the global competitiveness of Australian firms. By way of example, our current direct taxation system is high by international standards, and therefore remains an impediment to global investment in the country.

In order to achieve a more efficient and competitive taxation system, PECA supports a rigorous and comprehensive review of the Australian taxation system with the aim of creating a more

30 Western Australian Department of Resources Development, submission no. 37, p.7.

31 AMEC, submission no. 25, pp. 8-9.

dynamic, internationally competitive and equitable system that will support investment, growth and job creation.³²

- 6.58 Industry, however, was generally supportive of the direction of tax reform in Australia in recent years including the overall outcome of the recent business tax review. However, some, particularly those from the mining sector, expressed concern at the elimination of accelerated depreciation during this process. AMEC suggested that:

We believe that government has, in its business reform package, done as well as one could have expected it to have done with such a broad-ranging inquiry and we are, except in the case of one issue, very satisfied with the fairness of the package. The one issue which we are quite concerned about, because it goes to something dear to our heart which is business investment, is the rather muddled way that accelerated depreciation has been treated.³³

- 6.59 While understanding the mining industry's concern over the removal of accelerated depreciation, the Committee notes that this is more of a concern for some companies than others. As suggested by the Minerals Council of Australia in response to a question on whether the package will assist value-adding:

It is a project by project evaluation of different investment decisions. The lowering of the company tax rate will obviously make it more attractive for some companies to invest here. On the other hand, in regional Australia where up to 50 per cent of a project development cost is in infrastructure, it may work against that in terms of the removal of accelerated depreciation....But, overall, we think it is a pragmatic outcome. We think that the balance that has been struck will still encourage investment here in Australia.³⁴

- 6.60 Other tax related issues that received significant attention during the Committee's inquiry include the R&D taxation concession and the investment allowance.

- 6.61 On the issue of the R&D tax concession, the concerns expressed centred on the 1996 reduction in the allowance from 150 to 125 per cent and on the impact on the concession of the recent decision to reduce the company tax rate. With regard to the first of these issues, the Association of Mining and Exploration Companies claimed:

32 PECA, submission no. 16, p. 2.

33 Mr Savell, Association of Mining and Exploration Companies, transcript of evidence, p. 108.

34 Mr Wells, Minerals Council of Australia, transcript of evidence, p. 35.

The Australian mining industry is at the technological forefront in world terms. Despite comprising a relatively high cost country in which to operate, Australian technical expertise, coupled with a previously robust R&D taxation deduction, provided a means for many Australian mining companies to significantly expand their domestic mineral exploration and mining related research and activities. The 1996 reduction in the R&D tax concession has however, removed a substantial incentive to further expand industry activities in Australia.³⁵

6.62 On the question of the impact of the reduced company tax rate, the Chamber of Minerals and Energy of Western Australia suggested:

In discussions with the government prior to the government's response to the tax package being released, we made representations to at least maintain in real terms the 125 per cent R&D concession. Of course, moving to a 30 per cent tax rate lowers in real terms the 125 per cent. So we thought the government had listened well - there were heads nodding - but it did not translate to the package, unfortunately, so there is further erosion of the R&D tax concession.³⁶

6.63 The reduction in the company tax rate undoubtedly increases the attractiveness of investing in Australia. However, the cut in the R&D tax concession - from 150 per cent to 125 per cent - may well have reduced the attractiveness of investing in R&D compared with other forms of investment. Taking the company tax rate reduction as a given, the Committee accepts that investment in research into raw materials processing would be higher with a 150 per cent R&D tax concession than with a 125 per cent concession.

6.64 Further discussion of the recent developments in the R&D tax concession is provided in the Committee's August 1999 report on *The Effect of Certain Public Policy Changes on Australia's R&D*.

6.65 The concerns expressed about investment incentives during the inquiry centred on the claim that other countries offer attractive incentives to encourage new or expanded industries, while Australian industry receives comparatively little support. The Process Engineers and Constructors Association, for instance, suggested:

In the competition for investment funds, Australia is competing against many countries that have strong investment incentives. In

35 AMEC, submission no. 25, p.17.

36 Mr Satchwell, Chamber of Minerals and Energy of Western Australia, transcript of evidence, p.150.

particular, many countries in Asia, against whom we compete directly, offer tax concessions for new investments....

These incentives are very attractive to capital intensive industries, and compensate in part for the large capital outlays required upfront. In return for these incentives, these large projects create not only direct output and employment, but a whole chain of secondary effects in support industry development, the generation of export earnings and taxation revenue.³⁷

- 6.66 While accepting that the incentives offered by these countries could divert investment in raw materials processing away from Australia, the Committee notes that the Commonwealth and State Governments also offer some incentives for potential projects.
- 6.67 The Commonwealth Government, for example, recently announced as part of its business tax reform package that it would consider the provision of investment incentives to strategic investment projects in limited and special circumstances. These incentives will be considered on a case by case basis where the project would generate significant economic and employment benefits for Australia and could include grants, tax relief or the provision of infrastructure services.
- 6.68 The Committee will further consider the issue of an appropriate tax regime during the next stage of its inquiry and it therefore invites additional comment on this matter.

Impact of globalisation

- 6.69 The Committee also received a range of evidence on the impact of globalisation on value-adding activity in Australia, covering both positive and negative aspects of this development.
- 6.70 From the positive perspective, there was substantial evidence that globalisation has brought advantages to Australia in terms of market competition, the returns from Australian companies investing overseas, the availability of foreign capital and access to new technology, management skills and markets. The Minerals Council of Australia suggested:

To the extent that there is access to foreign markets as well, it is sometimes garnered. Take Japan, for example. There is a perception of security of supply that comes from Japanese companies participating in our market. The quid pro quo is a sense of security in terms of access to markets in difficult times by

having Japanese partners. It is a classic structure that you see all around the world.³⁸

- 6.71 There was, however, also evidence that foreign company control of technology, demand or Australian resources can have a negative impact on the development of value-adding industries. The CSIRO, for example, indicated:

The strength of large multinational companies in plant gene technologies is beginning to affect Australian agriculture. Outside the USA, Australia is the first country to commit to large-scale commercial planting of transgenic crops and this trend is expected to accelerate rapidly. However, it is the intellectual property holdings of these companies that are beginning to limit the operation of the Australian research providers for Australian agriculture....The consequence, now becoming evident, is that in many cases, these large companies are not willing to grant licences for their enabling technologies. In some cases this is because of litigation concerns....in other cases because they are still in the process of building their global business system strategies. Apart from the delay, it is unlikely that Australia will be able to feature as a significant player in most of these crops unless we invest in research programs that target complementary or competitive traits.³⁹

- 6.72 On the question of potential conflicts with customers, Iluka Resources indicated:

Mineral producers are the logical targets for policies to encourage downstream processing because the miners have access to resources. However, the options for mining companies can be complicated by the risk of competing with important customers. Most miners work hard to build up good relationships with their customers. These relationships will be strained if the miner wants to sell both raw materials and processed minerals to the customers' major markets. This problem underlines the need for commercial savoir-faire in adopting value-adding strategies.⁴⁰

- 6.73 The evidence was more mixed on the question of foreign ownership of local resources and the impact this has on investment in raw materials processing in Australia. While there are clear examples of foreign investors taking their raw materials to their existing overseas plants for processing, some witnesses claimed that it is competitiveness that largely

38 Mr Wells, Minerals Council of Australia, transcript of evidence, p. 42.

39 CSIRO, supplementary submission no. 22.1.

40 Iluka Resources, submission no. 33.

drives investment in new plant. A useful summary of this debate was provided by the Department of Agriculture, Fisheries and Forestry – Australia:

The mention you made of the possibility of multinational companies having an impact on this is something that comes up from time to time. As far as we can see, there are stories that go both ways. There is the issue of decisions being made about exports by large multinationals overseas that may disadvantage Australia. That is true, I suspect. Equally, though, we hear that those companies are quite ruthless about where they have things produced. If Australia can produce a commodity or a product more cheaply than that same company in another country, then that decision will be made to produce it in Australia. It cuts both ways.⁴¹

Regulatory issues

6.74 Inappropriate or inefficient government regulation was also put forward by a number of witnesses as a potential inhibitor to investment in value-adding activity. In addition to the questions discussed earlier in this chapter, the issues raised in this context generally covered two broad areas: the inconsistent regulations in different parts of Australia; and the regulations imposed on the production or marketing of various commodities.

6.75 The issue of inconsistency was discussed by the Minerals Council of Australia during the Committee's public hearings:

It does cause some confusion. We look for national consistency, not uniformity. We respect the role of the states and the state legislation which governs a lot of our projects - state mining legislation and so on. To give you an example, we have been driving hard to get some consistency in the principles that are applied to the management of safety in the industry across Australia. We have had varying systems and philosophies governing this which has caused some confusion. Through the ANZMEC ministers, we are working very hard to try to get national consistency. That is one small area.⁴²

41 Mr Wilson, AFFA, transcript of evidence, p. 63.

42 Mr Wells, Minerals Council of Australia, transcript of evidence, p. 35.

6.76 A number of criticisms were made regarding the regulations imposed on various commodities, including on electricity generation, aquaculture, wood, oil and gas, sugar and grains. For example, Goodman Fielder suggested:

In terms of contestability we believe that it is erroneous for statutory marketing authorities to seek a retention of single desk grain marketing arrangements based on a "community welfare" benefit from export activities. This argument largely ignores the implications of regulation on value adding industries within Australia (regional and urban). Further, a true assessment of contestability becomes subjective in the absence of the opportunity to have any effective competition against such marketing arrangements.

In this case we would contend the definition of community value has been confined to grain producers rather than the broader economy.⁴³

6.77 While it is not within the scope of this inquiry to analyse all the regulations that potentially influence the competitiveness of value-adding industries across Australia, these comments highlight the need to ensure government regulations are imposed in an efficient and appropriate manner.

6.78 There are valid reasons for imposing government regulations, but it also needs to be recognised that regulations can impose costs on industry and can work to inhibit investment and profitability.

6.79 Regulations should therefore only be imposed after a thorough study of all the implications, including the impact on industry at all levels. They should also be periodically examined to gauge the overall impact they are having on the community and to ensure that they still represent the most appropriate option for addressing the perceived problem.

6.80 Governments need to continue to work for greater uniformity of regulation across State and Territory boundaries. Inconsistent regulations can only work to increase industry costs and make investment in Australia, including in raw material processing projects, less competitive on the world scene.

43 Goodman Fielder, submission to the Productivity Commission inquiry into the Impact of Competition Policy Reforms on Rural and Regional Australia, attached to submission no. 3.

Infrastructure

6.81 Another impediment to investment relates to the question of infrastructure. Given that inadequate or inefficient infrastructure can have a significant impact on an industry's comparative advantage, several witnesses stressed the need for improved infrastructure in some areas, particularly in remote locations.

6.82 The importance of infrastructure to some mining entities was highlighted by the Minerals Council of Australia:

There is another distinguishing feature for our industry, and I mentioned it earlier. If you take a project like Murrin Murrin in Western Australia and the new laterite nickel project, about 50 per cent of their cost is actually in the infrastructure. It is in providing power, water, roads and rail.⁴⁴

6.83 The Minerals Council used this example to illustrate the need for considerate depreciation rates and to suggest that there is a case for using public funds in this area:

...in the remotest parts of Australia there is very little inducement. Certainly, there has been a tendency - and it is probably one of the few justifications for use of public funds to remove impediments - to provide infrastructure that would otherwise be provided by the public purse.⁴⁵

6.84 There was also significant focus during the inquiry on the need to have efficient and competitive infrastructure inputs, including in areas such as roads, energy, transport, communications and port facilities. While the provision of these services has been the subject of on-going microeconomic reform in recent times, and many of the services have been privatised, some witnesses believed further improvement was required.

6.85 The Horticultural Research and Development Corporation, for example, suggested:

Infrastructure issues such as inadequacies in the current domestic transport and international shipping systems are a current limitation to international competitiveness in the value-adding of Australian horticultural products. Continued waterfront reform and rationalisation of domestic transport are required if Australian industries are to become competitive in international markets.⁴⁶

44 Mr Wells, Minerals Council of Australia, transcript of evidence, p. 39.

45 *ibid.*

46 The Horticultural Research and Development Corporation, submission no. 24, p. 2.

- 6.86 Given the important part infrastructure plays in the competitiveness of raw materials processing industries, every effort needs to be made to ensure industry has access to efficient and effective infrastructure inputs.
- 6.87 The Committee notes that the House of Representatives Standing Committee on Primary Industries and Regional Services recently released the report of its inquiry into infrastructure and the development of Australia's regional areas, *Time Running Out: Shaping Regional Australia's Future*. The Committee will take the findings of this report into account during the next stage of its inquiry.
- 6.88 Much can be done to further encourage raw materials processing in Australia. While not every available mechanism will necessarily result in better economic and social outcomes for Australia, there are a range of options available to governments that are likely to help realise this objective.
- 6.89 The Committee believes that the Government should encourage raw materials processing in Australia by providing an environment that is conducive to investment and by working to remove impediments to this investment, including through:
- Providing a sound economic environment that is conducive to business investment and facilitates change;
 - Well-focused microeconomic reform;
 - Providing an efficient, consistent and balanced regulatory framework that recognises both the needs of industry and the wider social objectives;
 - Continuing with efforts to reduce the tariff and non-tariff barriers to trade with other nations;
 - Assisting local companies to identify export and investment opportunities and to establish themselves in overseas markets;
 - Encouraging research and development of new methods and techniques for undertaking raw materials processing; and
 - Encouraging productive labour relations and the continuing development of a skilled workforce.
- 6.90 The Committee would welcome further advice on these and other means of encouraging value-adding. The Committee will examine these issues in more detail during the next stage of the inquiry.